

PERAC AUDIT REPORT



Worcester Contributory Retirement System

JAN. 1, 2004 - DEC. 31, 2006



TABLE OF CONTENTS

| | |
|--|----|
| Letter from the Executive Director | 1 |
| Statement of Ledger Assets and Liabilities..... | 2 |
| Statement of Changes in Fund Balances | 3 |
| Statement of Receipts..... | 4 |
| Statement of Disbursements..... | 5 |
| Investment Income | 6 |
| Schedule of Allocation of Investments Owned..... | 7 |
| Supplementary Investment Regulations | 8 |
| <u>Notes to Financial Statements:</u> | |
| Note 1 - Summary of Plan Provisions | 17 |
| Note 2 - Significant Accounting Policies | 24 |
| Note 3 - Supplementary Membership Regulations..... | 25 |
| Note 4 - Administration of the System | 26 |
| Note 5 - Actuarial Valuation and Assumptions..... | 27 |
| Note 6 - Membership Exhibit..... | 28 |

PERAC

COMMONWEALTH OF MASSACHUSETTS | PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION COMMISSION

DOMENIC J. F. RUSSO, *Chairman* | A. JOSEPH DeNUCCI, *Vice Chairman*

MARY ANN BRADLEY | PAUL V. DOANE | KENNETH J. DONNELLY | JAMES M. MACHADO | DONALD R. MARQUIS

JOSEPH E. CONNARTON, *Executive Director*

September 26, 2007

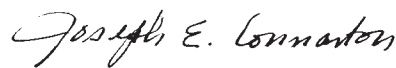
The Public Employee Retirement Administration Commission has completed an examination of the Worcester Retirement System pursuant to G.L. c. 32, § 21. The examination covered the period from January 1, 2004 to December 31, 2006. This audit was conducted in accordance with the accounting and management standards established by the Public Employee Retirement Administration Commission, in regulation 840 CMR 25.00. Additionally, all supplementary regulations approved by PERAC and on file at PERAC are listed in this report.

In our opinion the financial records are being maintained and the management functions are being performed in conformity with the standards established by the Public Employee Retirement Administration Commission. There were no significant findings to report.

We commend the Worcester Retirement Board for the exemplary operation of the system.

In closing, I acknowledge the work of examiner Richard Ackerson who conducted this examination, and express appreciation to the Board of Retirement and staff for their courtesy and cooperation.

Sincerely,



Joseph E. Connarton
Executive Director



STATEMENT OF LEDGER ASSETS AND LIABILITIES

| | AS OF DECEMBER 31, | | |
|--|----------------------|----------------------|----------------------|
| | 2006 | 2005 | 2004 |
| Net Assets Available For Benefits | | | |
| Cash | \$3,056,232 | \$8,758,160 | \$9,210,505 |
| Short Term Investments | 543,986 | 0 | 846,770 |
| Fixed Income Securities | 100,989,307 | 98,261,521 | 95,134,334 |
| Equities | 101,653,838 | 139,770,810 | 144,176,722 |
| Pooled Domestic Equity Funds | 157,157,017 | 115,022,851 | 113,711,946 |
| Pooled International Equity Funds | 155,937,243 | 114,737,675 | 105,059,762 |
| Pooled Domestic Fixed Income Funds | 28,896,926 | 18,756,638 | 32,158,883 |
| Pooled Global Fixed Income Funds | 9,677,217 | 25,812,560 | 25,780,320 |
| Pooled Alternative Investment Funds | 66,449,279 | 42,115,917 | 27,234,798 |
| Pooled Real Estate Funds | 86,013,550 | 80,211,050 | 52,479,214 |
| Interest Due and Accrued | 1,210,491 | 3,775,893 | 1,258,943 |
| Accounts Receivable | 9,119,075 | 3,086,397 | 2,121,818 |
| Accounts Payable | (3,907,393) | (6,292,968) | (3,074,399) |
| Total | <u>\$716,796,770</u> | <u>\$644,016,504</u> | <u>\$606,099,616</u> |
| Fund Balances: | | | |
| Annuity Savings Fund | \$138,456,863 | \$130,292,926 | \$122,748,771 |
| Annuity Reserve Fund | 48,226,093 | 48,729,409 | 49,481,572 |
| Pension Fund | 78,135,014 | 101,583,087 | 123,200,856 |
| Military Service Fund | 17,141 | 17,039 | 16,937 |
| Expense Fund | 0 | 0 | 0 |
| Pension Reserve Fund | 451,961,659 | 363,394,044 | 310,651,479 |
| Total | <u>\$716,796,770</u> | <u>\$644,016,504</u> | <u>\$606,099,616</u> |

STATEMENT OF CHANGES IN FUND BALANCES

| | Annuity Savings Fund | Annuity Reserve Fund | Pension Fund | Military Service Fund | Expense Fund | Pension Reserve Fund | Total All Funds |
|---------------------------|----------------------------|----------------------------|---------------------|-----------------------------|-----------------|----------------------------|-----------------------|
| Beginning Balance (2004) | \$115,779,891 | \$50,157,812 | \$145,817,209 | \$16,836 | \$0 | \$246,759,762 | \$558,531,510 |
| Receipts | 12,858,046 | 1,463,024 | 23,681,071 | 101 | 3,975,100 | 63,787,868 | 105,765,209 |
| Inter Fund Transfers | (4,057,200) | 3,964,346 | (10,994) | 0 | 0 | 103,849 | 0 |
| Disbursements | (1,831,965) | (6,103,610) | (46,286,429) | 0 | (3,975,100) | 0 | (58,197,103) |
| Ending Balance (2004) | 122,748,771 | 49,481,572 | 123,200,856 | 16,937 | 0 | 310,651,479 | 606,099,616 |
| Receipts | 13,234,602 | 1,562,568 | 26,595,123 | 102 | 4,062,968 | 52,626,338 | 98,081,702 |
| Inter Fund Transfers | (3,905,715) | 3,813,206 | (23,718) | 0 | 0 | 116,226 | 0 |
| Disbursements | (1,784,733) | (6,127,938) | (48,189,175) | 0 | (4,062,968) | 0 | (60,164,815) |
| Ending Balance (2005) | 130,292,926 | 48,729,409 | 101,583,087 | 17,039 | 0 | 363,394,044 | 644,016,504 |
| Receipts | 14,215,075 | 1,556,352 | 26,336,630 | 102 | 4,805,133 | 88,590,365 | 135,503,657 |
| Inter Fund Transfers | (4,260,693) | 4,291,728 | (8,286) | 0 | 0 | (22,749) | 0 |
| Disbursements | (1,790,445) | (6,351,396) | (49,776,417) | 0 | (4,805,133) | 0 | (62,723,391) |
| Ending Balance (2006) | <u>\$138,456,863</u> | <u>\$48,226,093</u> | <u>\$78,135,014</u> | <u>\$17,141</u> | <u>\$0</u> | <u>\$451,961,659</u> | <u>\$716,796,770</u> |

STATEMENT OF RECEIPTS

| | FOR THE PERIOD ENDING DECEMBER 31, | | |
|--|------------------------------------|---------------------|----------------------|
| | 2006 | 2005 | 2004 |
| Annuity Savings Fund: | | | |
| Members Deductions | \$12,774,114 | \$11,912,640 | \$11,759,090 |
| Transfers from Other Systems | 594,673 | 439,787 | 227,224 |
| Member Make Up Payments and Re-deposits | 55,137 | 100,470 | 200,895 |
| Member Payments from Rollovers | 24,385 | 56,716 | 0 |
| Investment Income Credited to Member Accounts | <u>766,766</u> | <u>724,988</u> | <u>670,837</u> |
| Sub Total | <u>14,215,075</u> | <u>13,234,602</u> | <u>12,858,046</u> |
| Annuity Reserve Fund: | | | |
| Investment Income Credited to the Annuity Reserve Fund | <u>1,556,352</u> | <u>1,562,568</u> | <u>1,463,024</u> |
| Pension Fund: | | | |
| 3 (8) (c) Reimbursements from Other Systems | 351,972 | 350,243 | 389,308 |
| Received from Commonwealth for COLA and Survivor Benefits | 2,630,055 | 2,665,402 | 3,141,385 |
| Pension Fund Appropriation | <u>23,354,603</u> | <u>23,579,478</u> | <u>20,150,377</u> |
| Sub Total | <u>26,336,630</u> | <u>26,595,123</u> | <u>23,681,071</u> |
| Military Service Fund: | | | |
| Contribution Received from Municipality on Account of Military Service | 0 | 0 | 0 |
| Investment Income Credited to the Military Service Fund | <u>102</u> | <u>102</u> | <u>101</u> |
| Sub Total | <u>102</u> | <u>102</u> | <u>101</u> |
| Expense Fund: | | | |
| Expense Fund Appropriation | 0 | 0 | 0 |
| Investment Income Credited to the Expense Fund | <u>4,805,133</u> | <u>4,062,968</u> | <u>3,975,100</u> |
| Sub Total | <u>4,805,133</u> | <u>4,062,968</u> | <u>3,975,100</u> |
| Pension Reserve Fund: | | | |
| Federal Grant Reimbursement | 0 | 0 | 0 |
| Pension Reserve Appropriation | 0 | 0 | 0 |
| Interest Not Refunded | 15,676 | 20,114 | 16,640 |
| Miscellaneous Income | 10 | 188 | 211 |
| Excess Investment Income | <u>88,574,680</u> | <u>52,606,037</u> | <u>63,771,017</u> |
| Sub Total | <u>88,590,365</u> | <u>52,626,338</u> | <u>63,787,868</u> |
| Total Receipts | <u>\$135,503,657</u> | <u>\$98,081,702</u> | <u>\$105,765,209</u> |

STATEMENT OF DISBURSEMENTS

| FOR THE PERIOD ENDING DECEMBER 31, | | | |
|--|---------------------|---------------------|---------------------|
| | 2006 | 2005 | 2004 |
| Annuity Savings Fund: | | | |
| Refunds to Members | \$949,439 | \$1,180,197 | \$1,337,552 |
| Transfers to Other Systems | <u>841,005</u> | <u>604,536</u> | <u>494,412</u> |
| Sub Total | <u>1,790,445</u> | <u>1,784,733</u> | <u>1,831,965</u> |
| Annuity Reserve Fund: | | | |
| Annuities Paid | 6,204,839 | 6,041,913 | 5,877,557 |
| Option B Refunds | <u>146,557</u> | <u>86,025</u> | <u>226,052</u> |
| Sub Total | <u>6,351,396</u> | <u>6,127,938</u> | <u>6,103,610</u> |
| Pension Fund: | | | |
| Pensions Paid: | | | |
| Regular Pension Payments | 23,016,975 | 22,855,516 | 22,505,297 |
| Survivorship Payments | 2,086,434 | 1,965,880 | 2,158,826 |
| Ordinary Disability Payments | 645,979 | 570,800 | 525,001 |
| Accidental Disability Payments | 9,636,053 | 9,225,437 | 8,667,939 |
| Accidental Death Payments | 2,595,181 | 2,610,195 | 2,595,290 |
| Section 101 Benefits | 171,814 | 168,440 | 165,151 |
| 3 (8) (c) Reimbursements to Other Systems | 2,777,733 | 2,211,530 | 1,872,944 |
| State Reimbursable COLA's Paid | 8,846,248 | 8,581,377 | 7,795,981 |
| Chapter 389 Beneficiary Increase Paid | <u>0</u> | <u>0</u> | <u>0</u> |
| Sub Total | <u>49,776,417</u> | <u>48,189,175</u> | <u>46,286,429</u> |
| Military Service Fund: | | | |
| Return to Municipality for Members Who Withdrew Their Funds | <u>0</u> | <u>0</u> | <u>0</u> |
| Expense Fund: | | | |
| Board Member Stipend | 15,000 | 15,000 | 15,000 |
| Salaries | 327,715 | 299,228 | 304,712 |
| Legal Expenses | 105,956 | 90,781 | 95,859 |
| Medical Expenses | 1,456 | 201 | 235 |
| Travel Expenses | 5,410 | 11,756 | 7,372 |
| Administrative Expenses | 132,099 | 103,625 | 65,416 |
| Furniture and Equipment | 3,021 | 2,871 | 0 |
| Management Fees | 3,714,634 | 3,112,141 | 3,003,844 |
| Custodial Fees | 336,851 | 273,046 | 324,281 |
| Consultant Fees | 132,000 | 121,000 | 128,897 |
| Fiduciary Insurance | <u>30,990</u> | <u>33,320</u> | <u>29,484</u> |
| Sub Total | <u>4,805,133</u> | <u>4,062,968</u> | <u>3,975,100</u> |
| Total Disbursements | <u>\$62,723,391</u> | <u>\$60,164,815</u> | <u>\$58,197,103</u> |

INVESTMENT INCOME

| | FOR THE PERIOD ENDING DECEMBER 31, | | |
|--|------------------------------------|---------------------|---------------------|
| | 2006 | 2005 | 2004 |
| Investment Income Received From: | | | |
| Cash | \$203,029 | \$141,200 | \$44,352 |
| Short Term Investments | 5,223 | 11,166 | 28,165 |
| Fixed Income | 5,279,303 | 5,375,369 | 5,246,484 |
| Equities | 1,480,048 | 1,897,445 | 1,713,921 |
| Pooled or Mutual Funds | 3,513,763 | 3,811,906 | 3,308,115 |
| Commission Recapture | 13,898 | 3,983 | 15,623 |
| Total Investment Income | <u>10,495,264</u> | <u>11,241,069</u> | <u>10,356,661</u> |
| Plus: | | | |
| Realized Gains | 79,004,869 | 29,469,505 | 21,874,847 |
| Unrealized Gains | 85,499,017 | 58,236,403 | 68,276,668 |
| Interest Due and Accrued on Fixed Income Securities - Current Year | <u>1,210,491</u> | <u>3,775,893</u> | <u>1,258,943</u> |
| Sub Total | <u>165,714,377</u> | <u>91,481,801</u> | <u>91,410,458</u> |
| Less: | | | |
| Paid Accrued Interest on Fixed Income Securities | (550,355) | (526,800) | (621,896) |
| Realized Loss | (9,244,365) | (9,861,770) | (12,260,364) |
| Unrealized Loss | (66,935,995) | (32,118,694) | (17,862,709) |
| Interest Due and Accrued on Fixed Income Securities - Prior Year | <u>(3,775,893)</u> | <u>(1,258,943)</u> | <u>(1,142,072)</u> |
| Sub Total | <u>(80,506,608)</u> | <u>(43,766,207)</u> | <u>(31,887,040)</u> |
| Net Investment Income | <u>95,703,033</u> | <u>58,956,664</u> | <u>69,880,079</u> |
| Income Required: | | | |
| Annuity Savings Fund | 766,766 | 724,988 | 670,837 |
| Annuity Reserve Fund | 1,556,352 | 1,562,568 | 1,463,024 |
| Military Service Fund | 102 | 102 | 101 |
| Expense Fund | <u>4,805,133</u> | <u>4,062,968</u> | <u>3,975,100</u> |
| Total Income Required | <u>7,128,354</u> | <u>6,350,627</u> | <u>6,109,062</u> |
| Net Investment Income | <u>95,703,033</u> | <u>58,956,664</u> | <u>69,880,079</u> |
| Less: Total Income Required | <u>7,128,354</u> | <u>6,350,627</u> | <u>6,109,062</u> |
| Excess Income To The Pension Reserve Fund | <u>\$88,574,680</u> | <u>\$52,606,037</u> | <u>\$63,771,017</u> |

SCHEDULE OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

| AS OF DECEMBER 31, 2006 | | | |
|-------------------------------------|----------------------|----------------------------------|-----------------------|
| | MARKET VALUE | PERCENTAGE OF TOTAL ASSETS | PERCENTAGE ALLOWED |
| Cash | \$3,056,232 | 0.4% | 100% |
| Short Term | 543,986 | 0.1% | 100% |
| Fixed Income | 100,989,307 | 14.2% | 20-80% |
| Equities | 101,653,838 | 14.3% | 70% |
| Pooled Domestic Equity Funds | 157,157,017 | 22.1% | 70% |
| Pooled International Equity Funds | 155,937,243 | 22.0% | 25% |
| Pooled Domestic Fixed Income Funds | 28,896,926 | 4.1% | 20-80% |
| Pooled Global Fixed Income Funds | 9,677,217 | 1.4% | 20-80% |
| Pooled Alternative Investment Funds | 66,449,279 | 9.4% | 7.5% |
| Pooled Real Estate Funds | 86,013,550 | 12.1% | 10% |
| Grand Total | <u>\$710,374,597</u> | <u>100.0%</u> | |

For the year ending December 31, 2006, the rate of return for the investments of the Worcester Retirement System was 15.00%. For the five-year period ending December 31, 2006, the rate of return for the investments of the Worcester Retirement System averaged 10.79%. For the 22-year period ending December 31, 2006, since PERAC began evaluating the returns of the retirement systems, the rate of return on the investments of the Worcester Retirement System was 10.95%.

SUPPLEMENTARY INVESTMENT REGULATIONS

The Worcester Retirement System submitted the following supplementary investment regulations, which were approved by PERAC on:

March 6, 1991

20.07(9) Commingled real estate equity funds shall not exceed 10% of the total book value of the portfolio at the time of purchase provided that:

- (a) the board does not participate in the selection of personnel responsible for making real estate investments and should this be required, prior to any participation by the board, the board shall consult with PERA to determine the appropriate course of action, and
- (b) such personnel retain authority in the decision making process, and
- (c) should an investment in a separate account result in the direct ownership of real estate, such shall be permitted only until such time as divestiture is prudent.

June 5, 1991

16.02(3) The Board may incur expenses for investment advice or management of the funds of the system by a qualified investment manager and the board may incur expenses for consulting services, which may include asset allocation studies, investment manager searches and on-going evaluation, trade analysis, performance evaluation and custodian bank searches, provided that any such consultant is registered as an investment adviser pursuant to the Investment Advisers Act of 1940. Such expenses may be charged against earned income from investments provided that the total of such expenses shall not exceed in any one year:

- (a) 1% of the value of the fund for the first 4% million; and
- (b) 0.5% of the value of the fund in excess of \$5 million.

16.02(4) The board may employ a custodian bank and may charge such expenses against earned income from investments provided that such expenses shall not exceed in any one-year .08% of the value of the fund.

March 11, 1992

20.09(1) Venture capital investments shall not exceed 3% of the total market value of the portfolio at the time of the investment provided that in any system with assets in excess of nineteen million dollars, venture capital investments may be made up to an amount equal to 5% of the total market value of the portfolio at the time of investment, shall be considered a separate asset class, and provided further that;

- (a) the board does not participate in the selection of the personnel responsible for making venture capital investments or otherwise exercise discretion in business affairs, and should this be required, prior to any participation by the board, the board shall consult with PERA to determine the appropriate course of action;
- (b) such personnel retain authority in the decision making process; and
- (c) should an investment in venture capital result in the direct ownership of securities, such shall be permitted only until such time as divestiture is prudent.

20.09(2) Venture capital investments shall only be made in venture capital funds operated by venture capital firms having their principal places of business in the United States.

20.09(3) All venture capital investments shall be made in companies which have their principal places of business in the United States.

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

April 6, 1992

20.07(6) Turnover of equity investments shall not exceed 100%, annually, as measured by the greater of purchases or sales relative to beginning market value.

February 4, 1993

20.04(1) United States based corporations, equities of foreign corporations, and fixed income Canadian securities, provided that:

(a) all such Canadian securities are denominated in U.S. currency and issued and traded in U.S. markets, and the total of all such securities shall be considered part of the board's fixed income asset allocation and shall not exceed 5% of the total market value of the portfolio.

20.04(6) American Depositary Receipts denominated in U.S. currency and listed in the New York Stock Exchange, provided that the total of all such investments shall be considered part of the board's equity asset allocation and shall not exceed 5% of the total market value of the portfolio.

October 12, 1995

20.06(2) Bonds shall have a minimum quality rating of Baa or equivalent as rated by one or more recognized bond rating services, however, 6% of the market value of the total portfolio may be invested in bonds with a minimum quality rating of B or equivalent as rated by one or more recognized bond rating services.

20.06(4) Fixed income holdings which are downgraded by one or more recognized rating services to below a Baa or equivalent rating must be sold within a reasonable period of time not to exceed one year, however, 6% of the market value of the total portfolio may be invested in bonds with a minimum quality rating of B or equivalent.

January 25, 1996

20.08(e) Enrollment in the Securities Lending Program offered by UBS Securities LLC provided that the lending of securities is limited to brokers, dealers, and financial institutions and that the loan is collateralized by cash or United States Government securities according to applicable regulatory requirements.

November 6, 1996

20.03(2) At least 20% but no more than 80% of the total portfolio valued at market shall consist of fixed income investments with a maturity of more than one year including international fixed income investments which shall be limited to 15% of the total portfolio valued at market, [(subject to 20.03(4))] and Yankee Bonds which shall be limited to 5% of the total fixed income portfolio valued at market.

June 11, 1997

20.03(1) Equity investments shall not exceed 70% of the total portfolio valued at market, including international equities, which shall not exceed 20% of the total portfolio valued at market. (Subject to CMR 20.03(4))

20.03(4) International investments shall not exceed 25% of the total portfolio valued at market.

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

October 5, 1999

16.8 In accordance with PERAC Investment Guideline 99-3, the Worcester Retirement Board may invest in Ascent Venture Partners III, L.P. The system is an investor in Ascent Venture Partners II, L.P. and has submitted the required documentation to justify investing in Ascent Venture Partners III.

March 20, 2000

16.08 In accordance with PERAC Investment Guideline 99-3, the Worcester Retirement System may invest in Boston Millennia Partners II, L.P. The System has not been invested in Boston Millennia Partners (BMP) I but information provided by the System, by the System's Investment Consultant, and by the manager indicates that BMP II can be reasonably considered a successor fund to one of the System's existing funds, Boston Capital Ventures (BCV) III. The general partners and other key managers of BMP are essentially the same team that managed BCV III. These men, led by Managing General Partner Dana Callow, Jr., created BMP in 1997, working initially in the same office space, and still maintain management responsibility for the investments in BVC III. Also, the investment objective of BMP II is the same as for BCV III.

April 6, 2000

16.08 In accordance with PERAC Investment Guideline 99-2, the Worcester Retirement Board may re-allocate 50% of the assets currently invested in the SSGA S&P 500 Flagship Fund into the SSGA Equal Weighted S&P 500 Fund. Under this modification, the Board will be invested in the same universe of stocks but will reduce its exposure to large capitalization growth stocks and increase its exposure to the smaller stocks within the S&P 500 Index. The board believes this modification will decrease its exposure to stocks that may be over-valued and increase its exposure to stocks that may represent better value.

October 19, 2000

16.08 The Worcester Retirement System may invest in the Standard Life European Strategic Partners Fund. This is an alternative investments "fund-of-funds" in which, according to an agreement between the Board and Standard Life, decisions as to the actual selection of investment partnerships will be made by Standard Life in a process not overseen by the Board. The Board will periodically monitor the selection process used by Standard Life.

August 14, 2001

16.08 In accordance with Investment Guideline 99-2, the Worcester Retirement Board is authorized to modify its fixed income management mandate with Loomis Sayles. The existing mandate calls for Loomis to invest in "high yield" corporate bonds and lower-investment-grade corporate bonds in approximately equal amounts. In order to simplify the board's portfolio structure, the lower-investment-grade portion of the account will be eliminated and Loomis will

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

concentrate on high- yield bonds. The board has had a satisfactory relationship with Loomis Sayles for over five years and the firm is recognized within the industry as a leading manager of high-yield bonds.

June 13, 2001

16.08 In accordance with PERAC Investment Guideline 99-2, the Worcester Retirement Board may modify its international equity mandate with The Boston Company. The Board currently invests in TBC's International Equity Pooled Fund and TBC makes small tactical allocations to emerging markets through its Emerging Markets Pooled Fund. TBC has created a single commingled fund, the Pooled Employees International ACWI (ex U.S.) Equity Fund by which to accomplish the same investment strategy in a more efficient manner. The Board will incur no cost or change in fees by making this modification.

September 22, 2003

16.08 The Worcester Retirement Board is authorized to make a modest modification to its high-yield investment mandate with Loomis Sayles. This modification involves no change in the overall investment objective or in the account's benchmark. Under this modification, Loomis Sayles is authorized to invest in senior loans ("bank loans") up to 20% of the market value of the account. These are loans that are made by banks to the same universe of companies that comprises the high yield market. Because these loans are typically senior in the capital structure as well as secured by collateral, they typically have better default recovery rates and superior risk-adjusted performance than conventional high-yield bonds. Also, since these loans are adjustable-rate in nature, they have very little volatility from interest-rate changes. Thus, it is expected that the inclusion of senior loans will help to preserve principal and reduce volatility in the high-yield portfolio.

September 22, 2003

16.08 Under the terms of Investment Guideline 99-2, the Worcester Retirement System is authorized to make a minor modification to its investment-grade fixed income mandate with Opus Investment Management. Under this change, Opus will create a separate account for Treasury Inflation-Protected Securities (TIPS), a segment of the market included in the universe the firm currently manages. Since the United States has issued only ten offerings of TIPS bonds and the account will not require active management, Opus will manage this account for a fee of only 0.10% which is lower than the fee for the system's existing core bond account.

October 20, 2003

16.08 In accordance with PERAC Investment Guideline 99-3, the Worcester Retirement Board is authorized to invest in the Riverside Capital Appreciation Fund 2003. This is the immediate successor fund to the Riverside Capital Appreciation Fund 2000, in which the Board invested in

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

2001. The earlier fund has had strong performance to date and the new fund is to be managed by the same investment team and with the same investment objectives.

October 27, 2003

16.08 In accordance with PERAC Investment Guideline 99-3, the Worcester Retirement Board may invest in the Ascent Venture Partners IV Fund. The board has been an investor in Ascent's two predecessor funds and the investment results from those two partnerships have been satisfactory to date.

February 25, 2004

19.01(6) Notwithstanding the provisions of Public Employee Retirement Administration Commission regulations, the City of Worcester Retirement Board may invest funds of the City of Worcester Retirement System (the "System") with a real estate investment fund, as contemplated by 840 CMR 19.01(4)-(6), known as Heitman Value Partners, L.P. ("the Fund"), and while the funds of the System are so invested the assets of the System shall be deemed to include, for purposes of applying the rules set forth in 840 CMR 16.00 et seq. and 17.00 et seq.; the System's interest in the Fund but not any of the underlying assets of the Fund; provided that, at all times, the Fund qualifies as a "real estate operating company" or venture capital operating company" within the meaning of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), and the regulations promulgated hereunder, or the assets of the Fund otherwise would not be treated as subject to ERISA.

January 31, 2005

16.08 In accordance with Investment Guideline 99-2, the Worcester Retirement Board is authorized to make a modest modification to its large cap equity index mandate with State Street Global Advisors. Standard & Poor's has announced that it will be adopting a free-float methodology for all their U.S. equity indexes, with final implementation scheduled for September 2005. In order to help address concerns over the possible market impact of this rebalancing, S&P has created provisional indexes. In hopes of avoiding whatever market impacts might be caused by the full transformation later this year, the Worcester Retirement Board has decided to switch from SSGA's S&P 500 Index Fund to the SSGA S&P 500 Flagship Securities Lending Provisional Fund.

May 2, 2005

16.08 In accordance with PERAC Investment Guideline 99-3, the Worcester Retirement Board is authorized to invest in Charlesbank Equity Fund VI. The Board has been a satisfied investor in the predecessor fund, Charlesbank Equity Fund V.

May 6, 2005

19.01(6) Notwithstanding the provisions of Public Employee Retirement Administration Commission regulations, including 840 CMR 21.01(6), the City of Worcester Retirement Board may exercise its investment discretion to invest funds of the City of Worcester Retirement System (the "System") in the shares of a real estate investment trust known as Hancock

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

Timberland VII Inc. (the “Fund”), as contemplated by 840 CMR 19.01(6), and while funds of the System are invested in shares of the Fund, for purposes of applying the rules set forth in 840 CMR 16.00 et seq. and 17.00 et seq., investments of the System shall not be deemed to include any of the underlying assets of the Fund, but shall only include the shares of the Fund, and the Fund shall not be deemed to be an investment manager or fiduciary to the System; provided that at all times the Fund qualifies as a “real estate operating company” within the meaning of the Employee Retirement Security Act of 1974, as amended (“ERISA”) and the regulations promulgated there under, or the assets of the Fund are otherwise not treated as “plan assets” of the System.

June 24, 2005

16.08 In accordance with PERAC Investment Guideline 99-2, the Worcester Retirement Board is authorized to modify its large cap equity mandate with State Street Global Advisors by transferring assets from the S&P 500 Index Fund to the Russell 1000 Value and Russell 1000 Growth index funds. Together, the two Russell 1000 funds cover the same large cap universe as the S&P 500, but the separation into the two style-specific funds will offer the board greater flexibility to control risk, and to take advantage of opportunities, relative to its growth/value allocation.

October 19, 2005

19.01(8) The Worcester Retirement Board is authorized to increase the Board’s maximum allocation to alternative investments (venture capital, private equity, et. al.) from the current regulatory maximum of 5% of total portfolio assets at the time of investment to 10%. The Board’s current allocation is about 4% and it is unlikely that the allocation will rise as high as 10%. Nevertheless, because of the special challenges involved in investing in this asset class, the Board would like the flexibility to exceed the existing 5% limit. The Board has had experience investing in alternative investments since 1992.

December 12, 2005

16.08 In accordance with Investment Guideline 99-3, the Worcester Retirement Board is authorized to invest in Northstar Mezzanine Partners IV. The system has been a satisfied investor in Northstar Mezzanine Partners III, the immediate predecessor fund, and has submitted updated Disclosure Statement and Exemption Application forms.

May 15, 2006

16.00, 17.00, 18.00, 19.00 and 21.00 Notwithstanding the provisions of 840 CMR 16.00 et seq., the Worcester Retirement Board may be permitted to invest funds of the Worcester Retirement System in BPIF Non-Taxable L.P., a Delaware limited partnership (the “Fund”), noting that as a so-called hedge fund of funds, the Fund invests in other funds, and while Blackstone Alternative Asset Management L.P., the Fund’s general partner (“General Partner”) can comply with the provisions of 840 CMR 16.00 et seq. with respect to the Fund’s direct investments, it cannot make such representations regarding any indirect investments, or the investments of the funds which it does not directly manage.

May 15, 2006

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

16.05 Notwithstanding the provisions of 840 CMR 16.00 et seq., the Worcester Retirement Board may be permitted to invest funds of the Worcester Retirement System in the funds known as Aetos Capital Multi-Strategy Arbitrage Cayman Fund, Aetos Capital Distressed Investment Strategies Cayman Fund, Aetos Capital Long/Short Strategies Cayman Fund and/or Aetos Capital Market Neutral Strategies Cayman Fund (collectively “Aetos Funds”) noting that as a so-called hedge fund of funds, the Aetos Funds do not trade securities, and therefore do not pay brokerage commissions or use soft dollars; and, the Aetos Funds do not vote proxies or participate in tender offers, because said Funds do not own individual securities.

June 26, 2006

16.08 In accordance with Investment Guideline 99-2, the Worcester Retirement Board is authorized to transfer its assets from TBC’s International ACWI (All Countries World Index) Fund to TBC’s EAFE Value Fund. The two funds are managed by the same portfolio management team and in a similar style, with the difference being that the ACWI Fund includes a small allocation to emerging market equities. Since the Board recently hired a separate manager dedicated to emerging market equities, the Board is making this change in order to avoid any overlap between the two managers. By slightly limiting its investment universe, the Boston Company will focus on international developed market equities while the newly hired manager will be responsible for emerging market equities.

August 30, 2006

16.08 In accordance with PERAC Investment Guideline 99-2, the Worcester Retirement Board is authorized to invest in State Street Global Advisors’ S&P 400 Index fund on a temporary basis. This mandate is to allow the Board to maintain its allocation to mid cap equity following the termination of The Boston Company. TBC had assigned a new portfolio manager to Worcester’s account about a year ago. The Board concluded at its August 22, 2006 meeting that it no longer had confidence in him as a result of badly lagging performance and significantly greater volatility than anticipated. The Board currently has three index fund accounts with SSgA and has been very satisfied with its relationship with the firm. This temporary mandate will expire on December 29, 2006.

December 4, 2006

16.08 In accordance with Investment Guideline 99-3, the Worcester Retirement Board is authorized to invest in the Standard Life European Strategic Partners Fund 2006. The Board has been a satisfied investor in Standard Life’s first ESP Fund (2000) and the basic strategy as well as the management team are essentially the same. The manager has submitted the required updated regulatory documents.

December 4, 2006

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

16.08 In accordance with Investment Guideline 99-3, the Worcester Retirement Board is authorized to invest in the Riverside Capital Europe Fund III. The Board has been a satisfied investor in two of Riverside's preceding domestic buyout funds, both of which have produced impressive returns to date. The new fund focuses on European rather than domestic investments but the Board and its consultant have decided that this investment is appropriate because of:

1. the strong results from the two domestic buyout funds that the Board has invested in
2. the impressive performance of Riverside's previous European buyout fund,
3. the basic investment process and strategy is the same, and
4. most importantly, the same management team that has overseen the domestic operations also oversees the European operations.

February 13, 2007

Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Worcester Retirement Board may invest funds of the Retirement System (the "System") in the fund known as INVESCO Core Real Estate USA, LLC (the "Fund"), and effective as of the date of the initial investment by the System of any of its assets in the Fund, while the assets of the System are so invested, the assets of the System shall be deemed to include, for purposes of applying the rules set forth in 840 CMR 16.00 et seq. and 17.00 et seq., the System's interest in the Fund but not any of the underlying assets of the Fund; provided that, at all times, the Fund qualified as a "venture capital operating company" within the meaning of the Employee Retirement Income Security Act of 1974, as amended, and the regulations promulgated thereunder.

February 14, 2007

17.03 Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Worcester Retirement Board may invest funds of the Retirement System (the "System") in the fund known as the INVESCO U.S. Venture Partnership Fund III, LP (the "Fund"), and effective as of the date of the initial investment by the System of any of its assets in the Fund, while the assets of the System are so invested, the activities and investments of the Fund, and the underlying funds in which the Fund may invest, directly or indirectly, shall be deemed to satisfy the prohibited transaction rules set forth in 840 CMR 16.00 et seq. and 840 CMR 17.03 to the extent such activities satisfy the prohibited transaction rules set forth in Section 406 of the U.S. Employee Retirement Income Security Act of 1974, as amended ("ERISA"), taking into account statutory exemptions under ERISA, and Prohibited Transaction Class Exemption 84-14, as amended, and other available class exemptions.

February 15, 2007

17.03 Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Worcester Retirement Board may invest funds of the Retirement System (the "System") in the fund known as the INVESCO US Buyouts Partnership Fund II, LP (the "Fund"), and effective as of the date of the initial investment by the System of any of its assets in the Fund, while the assets of the System are so invested, the activities and investments of the Fund, and the underlying funds in which the Fund may invest, directly or indirectly, shall be deemed to satisfy the prohibited transaction rules set forth in 840 CMR 16.00 et seq. and 840

SUPPLEMENTARY INVESTMENT REGULATIONS (Continued)

CMR 17.03 to the extent such activities satisfy the prohibited transaction rules set forth in Section 406 of the U.S. Employee Retirement Income Security Act of 1974, as amended (“ERISA”), taking into account statutory exemptions under ERISA, and Prohibited Transaction Class Exemption 84-14, as amended, and other available class exemptions.

February 15, 2007

17.03 Notwithstanding the provisions of the Public Employee Retirement Administration Commission regulations, the Worcester Retirement Board may invest funds of the Retirement System (the “System”) in the fund known as the INVESCO Non-US Partnership Fund II, LP (the “Fund”), and effective as of the date of the initial investment by the System of any of its assets in the Fund, while the assets of the System are so invested, the activities and investments of the Fund, directly or indirectly, shall be deemed to satisfy the prohibited transaction rules set forth in 840 CMR 16.00 et seq. and 840 CMR 17.03 to the extent such activities satisfy the prohibited transaction rules set forth in Section 406 of the U.S. Employee Retirement Income Security Act of 1974, as amended (“ERISA”), taking into account statutory exemptions under ERISA, and Prohibited Transaction Class Exemption 84-14, as amended, and other available class exemptions.

February 21, 2007

16.08 In accordance with Investment Guideline 99-3, the Worcester Retirement Board is authorized to invest in Boston Millennia Partners III. The Board has been a satisfied investor in BMP’s predecessor partnership as well as in a previous venture partnership managed by this team while at a different firm. The management team remains intact and, after conducting due diligence on the firm, the board and its consultant are confident in BMP’s capabilities.

March 13, 2007

17.03 Notwithstanding the provisions of the Public Employee Retirement Administration Commission’s investment regulations, the Worcester Retirement Board may exercise its discretion to invest funds of the Worcester Retirement System (the “System”) in Harvest Partners V, L.P. (the “Fund”), as contemplated by 840 CMR 19.01(6), and while the funds of the System are invested in shares of the Fund, for purposes of applying the rules set forth in 840 CMR 16.00 et seq. and 17.00 et seq., investments of the System shall not be deemed to include any of the underlying assets of the Fund, but shall only include the shares of the Fund, and the Fund shall not be deemed to be an investment manager or fiduciary to the System; provided that the General Partner shall use its reasonable best efforts at all times to conduct the affairs of the Partnership such that the assets of the Partnership would not constitute plan assets of any ERISA partner subject to Title I of ERISA or Section 4975 of the Internal Revenue Code of 1986, as amended, pursuant to the United States Department of Labor at Section 2510.3-101 of Part 2510 of Chapter XXV, Title 29 of the Code of Federal Regulations.

NOTES TO FINANCIAL STATEMENTS

NOTE I – SUMMARY OF PLAN PROVISIONS

The plan is a contributory defined benefit plan covering all Worcester Retirement System member unit employees deemed eligible by the retirement board, with the exception of school department employees who serve in a teaching capacity. The Teachers' Retirement Board administers the pensions of such school employees.

ADMINISTRATION

There are 106 contributory Retirement Systems for public employees in Massachusetts. Each system is governed by a retirement board, and all boards, although operating independently, are governed by Chapter 32 of the Massachusetts General Laws. This law in general provides uniform benefits, uniform contribution requirements, and a uniform accounting and funds structure for all systems.

PARTICIPATION

Participation is mandatory for all full-time employees. Eligibility with respect to part-time, provisional, temporary, seasonal, or intermittent employment is governed by regulations promulgated by the retirement board, and approved by PERAC. Membership is optional for certain elected officials.

There are 3 classes of membership in the Retirement System:

Group 1:

General employees, including clerical, administrative, technical, and all other employees not otherwise classified.

Group 2:

Certain specified hazardous duty positions.

Group 4:

Police officers, firefighters, and other specified hazardous positions.

NOTES TO FINANCIAL STATEMENTS (Continued)

MEMBER CONTRIBUTIONS

Member contributions vary depending on the most recent date of membership:

| | |
|--------------------|---|
| Prior to 1975: | 5% of regular compensation |
| 1975 - 1983: | 7% of regular compensation |
| 1984 to 6/30/96: | 8% of regular compensation |
| 7/1/96 to present: | 9% of regular compensation |
| 1979 to present: | an additional 2% of regular compensation in excess of \$30,000. |

RATE OF INTEREST

Interest on regular deductions made after January 1, 1984 is a rate established by PERAC in consultation with the Commissioner of Banks. The rate is obtained from the average rates paid on individual savings accounts by a representative sample of at least 10 financial institutions.

RETIREMENT AGE

The mandatory retirement age for some Group 2 and Group 4 employees is age 65. Most Group 2 and Group 4 members may remain in service after reaching age 65. Group 4 members who are employed in certain public safety positions are required to retire at age 65. There is no mandatory retirement age for employees in Group 1.

SUPERANNUATION RETIREMENT

A member is eligible for a superannuation retirement allowance (service retirement) upon meeting the following conditions:

- completion of 20 years of service, or
- attainment of age 55 if hired prior to 1978, or if classified in Group 4, or
- attainment of age 55 with 10 years of service, if hired after 1978, and if classified in Group 1 or 2

NOTES TO FINANCIAL STATEMENTS (Continued)

AMOUNT OF BENEFIT

A member's annual allowance is determined by multiplying average salary by a benefit rate related to the member's age and job classification at retirement, and the resulting product by his creditable service. The amount determined by the benefit formula cannot exceed 80% of the member's highest three year average salary. For veterans as defined in G.L. c. 32, s. 1, there is an additional benefit of \$15 per year for each year of creditable service, up to a maximum of \$300.

- Salary is defined as gross regular compensation.
- Average Salary is the average annual rate of regular compensation received during the 3 consecutive years that produce the highest average, or, if greater, during the last three years (whether or not consecutive) preceding retirement.
- The Benefit Rate varies with the member's retirement age, but the highest rate of 2.5% applies to Group 1 employees who retire at or after age 65, Group 2 employees who retire at or after age 60, and to Group 4 employees who retire at or after age 55. A .1% reduction is applied for each year of age under the maximum age for the member's group. For Group 2 employees who terminate from service under age 55, the benefit rate for a Group 1 employee shall be used.

DEFERRED VESTED BENEFIT

A participant who has completed 10 or more years of creditable service is eligible for a deferred vested retirement benefit. Elected officials and others who were hired prior to 1978 may be vested after 6 years in accordance with G.L. c. 32, s. 10.

The participant's accrued benefit is payable commencing at age 55, or the completion of 20 years, or may be deferred until later at the participant's option.

WITHDRAWAL OF CONTRIBUTIONS

Member contributions may be withdrawn upon termination of employment. Employees who first become members on or after January 1, 1984, may receive only limited interest on their contributions if they voluntarily terminate their service. Those who leave service with less than 5 years receive no interest; those who leave service with greater than 5 but less than 10 years receive 50% of the interest credited.

NOTES TO FINANCIAL STATEMENTS (Continued)

DISABILITY RETIREMENT

The Massachusetts Retirement Plan provides 2 types of disability retirement benefits:

ORDINARY DISABILITY

Eligibility: Non-veterans who become totally and permanently disabled by reason of a non-job related condition with at least 10 years of creditable service (or 15 years creditable service in systems in which the local option contained in G.L. c. 32, s. 6(1) has not been adopted).

Veterans with ten years of creditable service who become totally and permanently disabled by reason of a non-job related condition prior to reaching "maximum age".

Retirement Allowance: Equal to the accrued superannuation retirement benefit as if the member was age 55. If the member is a veteran, the benefit is 50% of the member's final rate of salary during the preceding 12 months, plus an annuity based upon accumulated member contributions plus credited interest. If the member is over age 55, he or she will receive not less than the superannuation allowance to which he or she is entitled.

ACCIDENTAL DISABILITY

Eligibility: Applies to members who become permanently and totally unable to perform the essential duties of the position as a result of a personal injury sustained or hazard undergone while in the performance of duties. There are no minimum age or service requirements.

Retirement Allowance: 72% of salary plus an annuity based on accumulated member contributions, with interest. This amount is not to exceed 100% of pay. For those who became members in service after January 1, 1988 or who have not been members in service continually since that date, the amount is limited to 75% of pay. There is an additional pension of \$611.28 per year (or \$312.00 per year in systems in which the local option contained in G.L. c. 32, s. 7(2)(a)(iii) has not been adopted), per child who is under 18 at the time of the member's retirement, with no age limitation if the child is mentally or physically incapacitated from earning. The additional pension may continue up to age 22 for any child who is a full time student at an accredited educational institution.

NOTES TO FINANCIAL STATEMENTS (Continued)

ACCIDENTAL DEATH

Eligibility: Applies to members who die as a result of a work-related injury or if the member was retired for accidental disability and the death was the natural and proximate result of the injury or hazard undergone on account of which such member was retired.

Allowance: An immediate payment to a named beneficiary equal to the accumulated deductions at the time of death, plus a pension equal to 72% of current salary and payable to the surviving spouse, dependent children or the dependent parent, plus a supplement of \$312 per year, per child, payable to the spouse or legal guardian until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

The surviving spouse of a member of a police or fire department or any corrections officer who, under specific and limited circumstances detailed in the statute, suffers an accident and is killed or sustains injuries resulting in his death, may receive a pension equal to the maximum salary for the position held by the member upon his death.

In addition, an eligible family member may receive a one time payment of \$100,000.00 from the State Retirement Board.

DEATH AFTER ACCIDENTAL DISABILITY RETIREMENT

Effective November 7, 1996, Accidental Disability retirees were allowed to select Option C at retirement and provide a benefit for an eligible survivor. For Accidental Disability retirees prior to November 7, 1996, who could not select Option C, if the member's death is from a cause unrelated to the condition for which the member received accidental disability benefits, a surviving spouse will receive an annual allowance of \$6,000.

DEATH IN ACTIVE SERVICE

Allowance: An immediate allowance equal to that which would have been payable had the member retired and elected Option C on the day before his or her death. For death occurring prior to the member's superannuation retirement age, the age 55 benefit rate is used. The minimum annual allowance payable to the surviving spouse of a member in service who dies with at least two years of creditable service is \$3,000, provided that the member and the spouse were married for at least one year and living together on the member's date of death.

The surviving spouse of such a member in service receives an additional allowance equal to the sum of \$1,440 per year for the first child, and \$1,080 per year for each additional child until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

NOTES TO FINANCIAL STATEMENTS (Continued)

COST OF LIVING

If a system has accepted Chapter 17 of the Acts of 1997, and the Retirement Board votes to pay a cost of living increase for that year, the percentage is determined based on the increase in the Consumer Price Index used for indexing Social Security benefits, but cannot exceed 3.0%. Section 51 of Chapter 127 of the Acts of 1999, if accepted, allows boards to grant COLA increases greater than that determined by CPI but not to exceed 3.0%. The first \$12,000 of a retiree's total allowance is subject to a cost-of-living adjustment. The total Cost-of-Living adjustment for periods from 1981 through 1996 is paid for by the Commonwealth of Massachusetts.

METHODS OF PAYMENT

A member may elect to receive his or her retirement allowance in one of 3 forms of payment.

Option A: Total annual allowance, payable in monthly installments, commencing at retirement and terminating at the member's death.

Option B: A reduced annual allowance, payable in monthly installments, commencing at retirement and terminating at the death of the member, provided, however, that if the total amount of the annuity portion received by the member is less than the amount of his or her accumulated deductions, including interest, the difference or balance of his accumulated deductions will be paid in a lump sum to the retiree's beneficiary or beneficiaries of choice.

Option C: A reduced annual allowance, payable in monthly installments, commencing at retirement. At the death of the retired employee, 2/3 of the allowance is payable to the member's designated beneficiary (who may be the spouse, or former spouse who remains unmarried for a member whose retirement becomes effective on or after February 2, 1992, child, parent, sister, or brother of the employee) for the life of the beneficiary. For members who retired on or after January 12, 1988, if the beneficiary pre-deceases the retiree, the benefit payable increases (or "pops up") based on the factor used to determine the Option C benefit at retirement. For members who retired prior to January 12, 1988, if the System has accepted Section 288 of Chapter 194 of the Acts of 1998 and the beneficiary pre-deceases the retiree, the benefit payable "pops up" in the same fashion. The Option C became available to accidental disability retirees on November 7, 1996.

NOTES TO FINANCIAL STATEMENTS (Continued)

ALLOCATION OF PENSION COSTS

If a member's total creditable service was partly earned by employment in more than one retirement system, the cost of the "pension portion" is allocated between the different systems pro rata based on the member's service within each retirement system.

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The accounting records of the System are maintained on a calendar year basis in accordance with the standards and procedures established by the Public Employee Retirement Administration Commission.

The Annuity Savings Fund is the fund in which members' contributions are deposited. Voluntary contributions, re-deposits, and transfers to and from other systems, are also accounted for in this fund. Members' contributions to the fund earn interest at a rate determined by PERAC. Interest for some members who withdraw with less than ten years of service is transferred to the Pension Reserve Fund. Upon retirement, members' contributions and interest are transferred to the Annuity Reserve Fund. Dormant account balances must be transferred to the Pension Reserve Fund after a period of ten years of inactivity.

The Annuity Reserve Fund is the fund to which a member's account is transferred upon retirement from the Annuity Savings Fund and Special Military Service Credit Fund. The annuity portion of the retirement allowance is paid from this fund. Interest is credited monthly to this fund at the rate of 3% annually on the previous month's balance.

The Special Military Service Credit Fund contains contributions and interest for members while on a military leave for service in the Armed Forces who will receive creditable service for the period of that leave.

The Expense Fund contains amounts transferred from investment income for the purposes of administering the retirement system.

The Pension Fund contains the amounts appropriated by the governmental units as established by PERAC to pay the pension portion of each retirement allowance.

The Pension Reserve Fund contains amounts appropriated by the governmental units for the purposes of funding future retirement benefits. Any profit or loss realized on the sale or maturity of any investment or on the unrealized gain of a market valued investment as of the valuation date is credited to the Pension Reserve Fund. Additionally, any investment income in excess of the amount required to credit interest to the Annuity Savings Fund, Annuity Reserve Fund, and Special Military Service Credit Fund is credited to this Reserve account.

The Investment Income Account is credited with all income derived from interest and dividends of invested funds. At year-end the interest credited to the Annuity Savings Fund, Annuity Reserve Fund, Expense Fund, and Special Military Service Credit Fund is distributed from this account and the remaining balance is transferred to the Pension Reserve Fund.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS

The Worcester Retirement System submitted the following supplementary membership regulations, which were approved by PERAC on:

March 29, 1993

Membership

All part-time, provisional, temporary or intermittent employees who are regularly scheduled to work twenty (20) or more hours per week are required to become members of the Worcester Retirement System and to make weekly contributions to the system pursuant to G.L. c. 32, §22 (1)(b). Those employees who are not regularly scheduled to work at least twenty (20) hours per week will not be allowed membership in the Worcester Retirement System.

February 17, 1998

Recovery of Earnings

Recovery of earnings in excess of limitations set forth in M.G.L. c. 32, s. 91A. Disabled members of the Worcester Retirement System whose calendar year earnings exceed an amount which when added to the member's retirement allowance is greater than the amount of regular compensation which would have been payable to such member if such member had continued in service in the grade held by him at the time he was retired plus the sum of five thousand dollars, must refund to the Worcester Retirement System the amount of said over earnings in either a lump-sum or, in the alternative, if the member can demonstrate that a lump-sum payment would result in financial hardship, a monthly payment schedule of not more than six months, provided the member amply demonstrates financial hardship to the Board's satisfaction.

February 22, 1999

Payments Effective September 1, 1998 all retirement payments made by the Worcester Retirement System [may] be made by electronic funds transfer. This will be a direct deposit system and [may] apply to all amounts payable to Worcester Retirement Systems members and beneficiaries. This provision is not mandatory for any member or beneficiary of the Worcester Retirement System. The Worcester Retirement Boards will provide electric fund transfer notices to retirees when they first enroll in the program; any time there is a change in their monthly amount and at year-end (12/31).

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 4 - ADMINISTRATION OF THE SYSTEM

The System is administered by a five person Board of Retirement consisting of the City Auditor who shall be a member ex-officio, a second member appointed by the governing authority, a third and fourth member who shall be elected by the members in or retired from the service of such system, and a fifth member appointed by the other four board members.

Ex-officio Member: James DelSignore

Appointed Member: Stephen Wentzell Term Expires: Indefinite

Elected Member: Elizabeth Early Term Expires: 10/31/07

Elected Member: Raymond McGrath Term Expires: 12/31/08

Appointed Member: Thomas Wade Term Expires: 01/09/09

The Board members are required to meet at least once a month. The Board must keep a record of all of its proceedings. The Board must annually submit to the appropriate authority an estimate of the expenses of administration and cost of operation of the system. The board must annually file a financial statement of condition for the system with the Executive Director of PERAC.

The investment of the system's funds is the responsibility of the Board. All retirement allowances must be approved by the Retirement Board and are then submitted to the PERAC Actuary for verification prior to payment. All expenses incurred by the System must be approved by at least two members of the Board.

The following retirement board members and employees are bonded by an authorized agent representing a company licensed to do business in Massachusetts as follows:

| | | |
|------------------------|---|------------------------|
| Treasurer - Custodian: |) | |
| Ex-officio Member: |) | \$50,000,000 Fiduciary |
| Elected Member: |) | \$1,000,000 Dishonesty |
| Appointed Member: |) | MACRS Policy |
| Staff Employee: |) | |

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 5 - ACTUARIAL VALUATION AND ASSUMPTIONS

The most recent actuarial valuation of the System was prepared by the Segal Company as of January 1, 2007.

| | |
|---|----------------------|
| The actuarial liability for active members was | \$386,545,160 |
| The actuarial liability for retired members was | <u>451,063,073</u> |
| The total actuarial liability was | 837,608,233 |
| System assets as of that date were | <u>716,796,770</u> |
| The unfunded actuarial liability was | <u>\$120,811,463</u> |
| The ratio of system's assets to total actuarial liability was | 85.6% |
| As of that date the total covered employee payroll was | \$152,838,201 |

The normal cost for employees on that date was 8.62% of payroll

The normal cost for the employer was 5.45% of payroll

The principal actuarial assumptions used in the valuation are as follows:

Investment Return: 8.25% per annum
 Rate of Salary Increase: 5.00% per annum

GASB STATEMENT NO. 25, DISCLOSURE INFORMATION AS OF JANUARY 1, 2007

| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a % of Cov. Payroll ((b-a)/c) |
|--------------------------------|--|--|--------------------------------------|----------------------------|-----------------------------|--|
| 1/1/2007 | \$716,796,770 | \$837,608,233 | \$120,811,463 | 85.6% | \$152,838,201 | 79.0% |
| 1/1/2006 | \$644,016,504 | \$806,957,464 | \$162,940,960 | 79.8% | \$145,830,593 | 111.7% |
| 1/1/2005 | \$606,099,616 | \$771,948,311 | \$165,848,695 | 78.5% | \$147,123,606 | 112.7% |
| 1/1/2004 | \$577,123,067 | \$743,570,440 | \$166,447,373 | 77.6% | \$138,796,895 | 119.9% |

NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 6 - MEMBERSHIP EXHIBIT

| | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Retirement in Past Years | | | | | | | | | | |
| Superannuation | 61 | 76 | 53 | 77 | 63 | 196 | 89 | 59 | 71 | 65 |
| Ordinary Disability | 0 | 1 | 1 | 2 | 2 | 1 | 2 | 1 | 3 | 1 |
| Accidental Disability | 7 | 14 | 11 | 13 | 17 | 15 | 12 | 11 | 20 | 13 |
| Total Retirements | 68 | 91 | 65 | 92 | 82 | 212 | 103 | 71 | 94 | 79 |
| Total Retirees, Beneficiaries and Survivors | 2,994 | 2,985 | 2,979 | 2,946 | 2,905 | 2,995 | 2,991 | 2,967 | 2,977 | 2,890 |
| Total Active Members | 3,549 | 3,505 | 3,569 | 3,896 | 4,069 | 3,628 | 3,345 | 3,421 | 3,346 | 3,404 |
| Pension Payments | | | | | | | | | | |
| Superannuation | \$15,503,544 | \$15,810,293 | \$16,157,845 | \$16,423,542 | \$17,082,481 | \$18,332,032 | \$21,186,242 | \$22,505,297 | \$22,855,516 | \$23,016,975 |
| Survivor/Beneficiary Payments | 1,044,270 | 1,009,788 | 1,030,729 | 1,244,324 | 1,961,652 | 2,079,554 | 2,153,708 | 2,158,826 | 1,965,880 | 2,086,434 |
| Ordinary Disability | 554,302 | 557,948 | 572,867 | 430,916 | 397,687 | 436,372 | 404,987 | 525,001 | 570,800 | 645,979 |
| Accidental Disability | 6,647,358 | 6,791,764 | 6,903,287 | 7,354,476 | 7,475,156 | 8,096,443 | 8,301,378 | 8,667,939 | 9,225,437 | 9,636,053 |
| Other | 2,737,989 | 2,810,044 | 2,883,919 | 3,108,352 | 10,776,945 | 11,333,986 | 11,606,678 | 12,429,366 | 13,571,542 | 14,390,976 |
| Total Payments for Year | <u>\$26,487,463</u> | <u>\$26,979,837</u> | <u>\$27,548,647</u> | <u>\$28,561,610</u> | <u>\$37,693,921</u> | <u>\$40,278,388</u> | <u>\$43,652,993</u> | <u>\$46,286,429</u> | <u>\$48,189,175</u> | <u>\$49,776,417</u> |

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